PRAGER DREIFUSS

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New measures in case of imminent or identified over-indebtedness of companies

In our March 2020 newsletter we explained how companies can restructure and avoid bankruptcy if they run into payment difficulties due to COVID-19. In the meantime, the Federal Council has enacted new measures to protect companies in the event of imminent or identified over-indebtedness, which are explained in this newsletter.

1. Background

In Switzerland the Federal Council has issued a catalogue of restrictions (e.g. closure of publicly accessible facilities) based on the *COVID-19 Ordinance 2*.[1] These have considerable adverse effects and financial consequences for a large number of companies. In our newsletter of March 2020, we provided information on what companies can do if they run into payment difficulties and are threatened with bankruptcy despite having exhausted the emergency aid set up by the Federal Council. These include the debt-restructuring moratorium, the emergency moratorium and the stay of enforcement.

[1] To be found at https://www.admin.ch/opc/de/classified-compilation/20200744/index.html (status as of 17 April 2020)

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The Federal Council has decided to partially extend these protective measures or replace them with other, tailor-made instruments from 20 April 2020 for a period of six months. The measures are implemented by the *COVID-19-Verordnung Insolvenzrecht* dated 16 April 2020[2] and are explained below.

2. Measures in case of payment difficulties

2.1. Emergency moratorium

An expert opinion on behalf of the Federal Government concludes that the instrument of the emergency moratorium (*Notstundung*) is superfluous and therefore advises against declaring it applicable in the context of the corona crisis.[3] Instead, companies in financial difficulties should request a deferral via the new provisions on the debt-restructuring moratorium (see below, chapters 2.3. and 2.4).[4]

The instrument of emergency moratorium should therefore not be used in the context of the corona crisis.

2.2. Stay of enforcement

The general stay of enforcement ordered by the Federal Council on 18 March 2020[5] is problematic from various points of view.[6] The Swiss Federal Department of Justice and Police (FDJP) recognises this and points out that a long-term legal standstill could lead to serious disruptions of the entire economy.[7] With this in mind, the Federal Council has decided not to extend the standstill period when it expires on 19 April 2020.

An exception was discussed for the travel industry, which is struggling with considerable delays in the repayment of cancelled trips and for which an extension of the standstill period would be essential.[8] However, the Federal Council did not ultimately implement such stay of enforcement for the travel industry.

2.3. Modified moratorium

The purpose of the moratorium (sec. 293 et seq. DEBL) is to protect a debtor in financial difficulties from debt collection and to restructure the debtor's economic existence.

For a period of six months from 20 April 2020 the instrument of the moratorium has undergone certain adjustments. With the debtor's application for a moratorium, the submission of a provisional restructuring plan to the court is no longer required (sec. 3 para. 1 COVID-19-Verordnung Insolvenzrecht, cf. sec. 293 lit. a DEBL). Instead, the debtor's ability to restructure is checked by the administrator during the moratorium (see below).

Furthermore, the provisional debt-restructuring moratorium is extended from four to

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[2] To be found at https://www.bj.admin.ch/dam/data/bj/aktuell/news/2020/2020-04-16/vo-covid19-insolvenz-d.pdf

[3] Franco Lorandi, Gutachten dated 31 March 2020. To be found at https://www.bj.admin.ch/dam/data/bj/aktuell/coronavirus/beilage-4-gutachten-lorandi-d.pdf

[4] FDJP, Anpassungen im SchKG, dated 1 April 2020, p. 1.

[5] cf. Verordnung über den Rechtsstillstand gemäss Artikel 62 des Bundesgesetzes über Schuldbetreibung und Konkurs dated 18 March 2020, to be found at https://www.bj.admin.ch/dam/data/bj/aktuell/news/2020/2020-03-18/vo-d.pdf

[6] See our Newsletter of March 2020.

[7] See in detail FDJP, Konzeptpapier, dated 1 April 2020, p. 2 et seq., to be found at https://www.bj.admin.ch/dam/data/bj/aktuell/coronavirus/beilage-1-konzeptpapier-d.pdf

[8] vgl. Karin Kofler, Laura Frommberg. Streit um die Rückerstattung von Reisekosten. SonntagsZeitung, p. 29. 5 April 2020.

six months (sec. 4 COVID-19-Verordnung Insolvenzrecht). Finally, for the opening of bankruptcy ex officio to preserve the debtor's assets or because of the lack of prospect of a successful restructuring, a waiting period until the end of May 2020 applies provided the debtor was not over-indebted at the end of 2019 or creditors have subordinated their claims to the extent of the over-indebtendness (sec. 5 COVID-19-Verordnung Insolvenzrecht). At the end of the waiting period, the administrator checks the debtor's ability to restructure, and if the result is negative, he must submit a request to the court so that it can declare bankruptcy on the basis of sec. 296b DEBL.

2.4. COVID-19 deferral for SMEs

For SMEs, the initiation of a moratorium can be too costly. For SMEs, the legislator therefore provides a temporary instrument for a time-limited deferral with the introduction of the so-called COVID-19 deferral.

The COVID-19 deferral is similar to the provisional moratorium pursuant to sec. 293a et seq. DEBL, but it is designed as a simple and standardised mass procedure.

Prerequisites for the granting of the COVID-19 deferral by the judge are that the debtor was not already over-indebted by the end of 2019 (or creditors have subordinated their claims to the extent of the over-indebtendness according to sec. 725 para. 2 CO) and that the debtor is an SME (certain ratios may not be exceeded). This means that large companies, especially listed companies, cannot make use of the COVID-19 deferral.

Central provisions of the COVID-19 deferral are:

- Content: The deferral covers claims against the debtor that arose before the deferral was granted. These claims may not be paid by the debtor. An exception is made for first class claims, e.g. wage and alimony claims, which are excluded from the deferral (sec. 11 COVID-19-Verordnung Insolvenzrecht). Apart from that, the effects of the deferral largely correspond to those of the ordinary moratorium (cf. sec. 297 and 298 DEBL);

- Duration: Short deferral of three months with the possibility of an extension for a maximum of another three months (sec. 6 para. 1 und sec. 7 para. 1 COVID-19-Verordnung Insolvenzrecht);

- Administrator: In order to keep expenses low, the appointment of an administrator is generally waived (sec. 9 COVID-19-Verordnung Insolvenzrecht);

- Dispositions: the debtor can continue his business activities provided that no legitimate creditor interests are affected (sec. 13 COVID-19-Verordnung Insolvenzrecht);

- Announcement: The judge makes the COVID-19 deferral public (sec. 10 COVID-19-Verordnung Insolvenzrecht);

- Transfer to a moratorium: Half of the duration of the COVID-19 deferral can be transferred to a moratorium (e.g. to conclude a composition agreement, which is not the aim of the COVID-19 deferral, sec. 15 COVID-19-Verordnung Insolvenzrecht); and

- Effects under company law: With the application for COVID-19 deferral the organs of the company have fulfilled their duties according to sec. 725 para. 2 CO in relation to depositing the balance sheet (or sec. 820 and sec. 903 para. 2 CO) (sec. 8 COVID-19-Verordnung Insolvenzrecht, see also the next chapter).

2.5. Notification of the judge / depositing the balance sheet

In our newsletter of March 2020, we pointed out that in certain countries (Germany, Austria) the deadline for notifying the bankruptcy court (depositing the balance sheet) will be extended if the reason for insolvency is based on the consequences of the corona pandemic. In Germany, for example, the obligation to file for bankruptcy has now been suspended until September 30, 2020 due to the corona crisis. [9]

Switzerland has now also taken measures in this area. Specifically, if there are concerns of over-indebtedness, the board of directors must continue to have an interim balance sheet prepared at going-concern and liquidation values. It should be noted here that COVID-19 credits of less than CHF 0.5 million are not to be taken into account as debt capital for the calculation of over-indebtedness up to 31 March 2022.[10] This exception does not apply to COVID-19 loans over CHF 0.5 million.

Despite the fact that over-indebtedness has been established, the Board of Directors is not required to notify the court in accordance with sec. 725 para. 2 CO if the company was not already over-indebted at the end of 2019 and there is a prospect of the over-indebtedness being eliminated by 31 December 2020 (sec. 1 COVID-19-Verordnung Insolvenzrecht). The decision must be documented and justified in writing. Within the scope of application of the new standard, the audit of interim balance sheets to determine over-indebtedness by an approved auditor (cf. sec. 725 para. 2 CO) may also be waived. It is also clarified that there is no obligation for the auditor to notify the court of the over-indebtedness if the board of directors may waive it.

In practice, however, it will often be difficult for the board of directors to make a reliable forecast for eliminating over-indebtedness, as it is difficult to estimate how the economy and one's own company will develop after the end of the corona crisis. There is a great danger that a judge will retrospectively - when an unfavorable development of the company is known - assess the forecast for eliminating over-indebtedness as an insufficient basis for a decision by the board of directors. Careful justification and recording of the Board of Directors' decisions in minutes is therefore required.

In addition, the waiver to qualify COVID-19 loans under CHF 0.5 million as debt capital until 31 March 2022 leads to a state of legal uncertainty, as it is not clear whether these loans are to be treated as debt capital from 31 March 2022 onwards without exception or whether there will be a transitional arrangement for hardship cases. From the point of view of legal certainty, the regulations in Germany and Austria, which simply give the board of directors more time to report over-indebtedness (and thus solve the problem of over-indebtedness), are preferable.

[9] cf. BMJV, Insolvenzantragspflicht wird ausgesetzt, to be found at https://www.bmjv.de/DE/Themen/FokusThemen/Corona/Insolvenzantrag/Corona_Insolvenzantrag_node.html

[10] According to sec. 24 of the COVID-19-Solidarbürgschaftsverordnung dated 25 March 2020, to be found at https://www.admin.ch/opc/de/official-compilation/2020/1077.pdf

3. Conclusion

With the new measures in the event of imminent or identified over-indebtedness, the Federal Council has created the basis for comprehensive protection of companies from the consequences of corona-related payment difficulties. However, since there is no universal remedy for companies, it must be analysed individually which measures are appropriate in each specific case.

Furthermore, it must be carefully examined whether the prerequisites for a waiver of depositing the balance sheet are met, since liability risks exist for the board of directors.

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